

Letter of Findings: 04-20170735
Sales and Use Tax
For the Years 2013, 2014, and 2015

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Indiana Department of Revenue's official position concerning a specific set of facts and issues. This document is effective as of its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Indiana Medical Practice was properly assessed use tax on purchases of artificial dermal material because the property purchased did not fall within the exemption for purchases by medical practitioners.

ISSUE

I. Sales and Use Tax - Exemption - Licensed Medical Practice.

Authority: IC § 6-2.5-1-1; IC § 6-2.5-1-17; IC § 6-2.5-2-1; IC § 6-2.5-3-4; IC § 6-2.5-5-18; IC § 6-2.5-5-19; IC § 6-8.1-5-1; Fresenius USA Marketing, Inc. v. Ind. Dep't of State Revenue, 56 N.E.3d 734 (Ind. Tax Ct. 2016); Dep't of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); Ind. Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Sq. Amoco, Inc. v. Ind. Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Ind. Dep't of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96 (Ind. Ct. App. 1974); [45 IAC 2.2-3-4](#); [45 IAC 2.2-5-28](#); [45 IAC 2.2-5-36](#).

Taxpayer argues that its purchases of artificial dermal material were exempt from use tax.

STATEMENT OF FACTS

Taxpayer is a licensed medical practice in Indiana. The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records for tax years 2013, 2014, and 2015, and assessed Taxpayer additional use tax on the purchase of supplies used in Taxpayer's medical practice. The audit concluded that Taxpayer's purchases of various medical supplies and computer software were subject to use tax because Taxpayer purchased those items without paying sales tax at the time of purchase and did not self-assess use tax.

Taxpayer disagreed with a portion of the assessment related to the purchase of artificial dermal material used in wound repair surgeries, and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representatives explained the basis for its protest. This Letter of Findings results. Additional facts will be addressed below as necessary.

I. Sales and Use Tax - Exemption - Licensed Medical Practice.

DISCUSSION

Taxpayer protests the imposition of use tax on purchases of artificial dermal material, asserting that it qualifies for exemption as a medical device or drug purchased by a medical practitioner. Taxpayer uses the artificial dermal material as a skin substitute in wound repair surgeries. According to the package inserts for the products, patients must have a prescription for the artificial dermal material. Taxpayer's patients obtain the product from Taxpayer as part of the surgical procedure.

The audit report concluded that the artificial dermal material purchases at issue were included in the finding that "instruments, equipment, supplies, bandages, splints, and other office supplies" were taxable to Taxpayer as general purchases made by a licensed practitioner. Because Taxpayer did not pay sales tax at the time it purchased the property, the Department therefore assessed Taxpayer additional use tax in accordance with [45 IAC 2.2-3-4](#).

It must be noted that all tax assessments are prima facie evidence that the Department's claim for the tax is valid, and the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Sq. Amoco, Inc. v. Ind. Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007); Ind. Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012). Thus, the taxpayer is required to provide documentation explaining and supporting its challenge that the Department's assessment is wrong. Further, "[W]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to an agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" Dep't of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579, 583 (Ind. 2014). Thus all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

Indiana imposes a sales tax on retail transactions and a complementary use tax on tangible personal property that is stored, used, or consumed in the state. IC § 6-2.5-1-1 et seq. A person who acquires property in a retail transaction is liable for sales tax on the transaction. IC § 6-2.5-2-1(b). Generally, all purchases of tangible personal property are subject to sales or use tax unless an enumerated exemption from sales or use tax is applicable. An exemption from use tax is granted for transactions where the gross retail tax ("sales tax") was paid at the time of purchase pursuant to IC § 6-2.5-3-4. There are also additional exemptions from sales tax and use tax. A statute which provides a tax exemption, however, is strictly construed against the taxpayer. Indiana Dep't of State Revenue v. RCA Corp., 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." Id. at 101.

With respect to the taxability of tangible personal property purchased by a licensed medical practitioner, [45 IAC 2.2-5-36](#) states:

(a) The gross retail tax shall apply to the following purchase transactions made by licensed practitioners:

- (1) All office furniture, equipment and supplies.
- (2) Drugs of a type not requiring a prescription, when not purchased for resale.
- (3) **Surgical instruments, equipment and supplies.**
- (4) **Bandages, splints, and all other medical supplies consumed in professional use.**
- (5) X-Ray, diathermy, diagnostic equipment, or any other apparatus used in the practice of surgery or medicine.

(b) The purchase of items for resale by the physician or surgeon. In order to resell items the practitioner must be licensed as a retail merchant, and must quote the selling price of any items separately from the charge for professional service. (**Emphasis added**).

The exemption from gross retail tax for licensed medical practitioners is found in IC § 6-2.5-5-19(c) (July 1, 2015), which provides:

Transactions involving **drugs, insulin, oxygen, blood, and blood plasma** are exempt from the state gross retail tax if purchased by a licensed practitioner (as defined in [IC 6-2.5-1-21.5](#)) or a health care facility (as defined in [IC 16-18-2-161\(a\)](#)) for the purpose of:

- (1) direct consumption in treating patients; or
- (2) resale to a patient that the practitioner is treating, in the case of sales of legend or nonlegend drugs. (**Emphasis added**).

(See also IC § 6-2.5-5-19 (e) and (f) (Jan. 1, 2004), which was in effect for the first two years of the audit period).

Taxpayer argues that its purchases of artificial dermal material should be exempt from tax because the tissue may only be used by patients under the order of a licensed medical professional, and should therefore be considered tax exempt medical devices. However, Taxpayer's argument relies upon IC § 6-2.5-5-18(c) (July 1, 2015), which provides, in relevant part:

Transactions involving the following are exempt from the state gross retail tax if **the end user acquires the**

property upon a prescription or drug order (as defined in [IC 16-42-19-3](#)) **that is required by law for the transaction from a licensed practitioner:**

- (1) Durable medical equipment (including a repair or a replacement part).
- (2) Mobility enhancing equipment (including a repair or replacement part).
- (3) Prosthetic devices, including artificial limbs, orthopedic devices, dental prosthetic devices, eyeglasses, and contact lenses (and including a repair or a replacement part).
- (4) Other medical supplies or devices that are used exclusively for medical treatment of a medically diagnosed condition, including a medically diagnosed condition due to:**
 - (A) injury;**
 - (B) bodily dysfunction; or**
 - (C) surgery.**

(Emphasis added).

The statute Taxpayer's argument relies upon is inapplicable for two reasons. First, this statute was not in effect during most of the audit period. The previous version of IC § 6-2.5-5-18, in effect for tax year 2013 until June 30, 2015, provided, in relevant part:

- (a) Sales or rentals of durable medical equipment, mobility enhancing equipment, prosthetic devices, artificial limbs, orthopedic devices, dental prosthetic devices, eyeglasses, contact lenses, and other medical supplies and devices are exempt from the state gross retail tax, if the sales or rentals are prescribed by a person licensed to issue the prescription.

Since 2009, the Department has interpreted this exemption to apply only to sales made directly to patients with a prescription. See *Fresenius USA Marketing, Inc. v. Ind. Dep't of State Revenue*, 56 N.E.3d 734, 736 (Ind. Tax Ct. 2016) (citing Revenue Rulings # 2009-16 ST and # 2009-17 ST (Dec. 23, 2009); Revenue Rulings # 2010-01 ST and # 2010-02 ST (Mar. 24, 2010)). The Department has consistently ruled that the exemption under the prior version of IC § 6-2.5-5-18(a) does not apply to sales of medical equipment made to healthcare service providers for treating patients with a prescription. *Id.*

Second, the current version of IC § 6-2.5-5-18 (July 1, 2015) provides a sales tax exemption to the patient as the end user of certain medical supplies, not to the licensed medical practitioner that purchases the medical supplies. The acquisition of exempt property by a licensed medical practitioner is set forth in IC § 6-2.5-5-19, which provides an exemption from gross retail tax only for "drugs, insulin, oxygen, blood, and blood plasma."

During the hearing, Taxpayer also argued that the artificial dermal material should alternatively be considered a "drug" and therefore exempt under IC § 6-2.5-5-19. Taxpayer argued that the artificial dermal material is soaked in a solution containing drugs, and should therefore be considered a drug itself. However, IC § 6-2.5-1-17 defines "drug" as:

[A] compound, substance, or preparation and any component of a compound, substance, or preparation that is:

- (1) recognized in the official United States Pharmacopoeia, official Homeopathic Pharmacopoeia of the United States, or official National Formulary, and supplement to any of them;
- (2) intended for use in the diagnosis, cure, mitigation, treatment, or prevention of disease; or
- (3) intended to affect the structure or any function of the body.

The term does not include food and food ingredients, dietary supplements, or alcoholic beverages.

The artificial dermal material purchased by Taxpayer does not fit within the definition of a drug, and is more properly classified as "other medical supplies or devices" under IC § 6-2.5-5-18(c)(4). The term "medical

equipment, supplies or devices" consists of "those items, the use of which is directly required to correct or alleviate injury to malfunction of, or removal of a portion of the purchaser's body." [45 IAC 2.2-5-28](#)(h). The products at issue are used during surgical procedures performed by Taxpayer to treat a bodily dysfunction within its patients. While this use is not taxable to the patient as the end user, it is taxable use by Taxpayer in accordance with [45 IAC 2.2-5-36](#)(a).

Taxpayer has not met its burden under [IC 6-8.1-5-1](#)(c) of showing that the Department's assessment was incorrect. Therefore, Taxpayer's protest must be denied.

FINDING

Taxpayer's protest is respectfully denied.

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